



Michigan Consumers
for Healthcare

Questions for Blue Cross & other supporters of this deal

Board Creation:

- To whom will the board of directors be accountable?
- To what extent and in what manner will Blue Cross's policyholders have authority over the board of directors?
- Will the initial board of directors be different from the current board members? Who will have the authority to nominate board members? Will policyholders have the ability to nominate board members and, if so, what will be the criteria?

Conversion:

- Why is it so urgent for Blue Cross to convert before the ACA takes effect? How do you reconcile your claims with the fact that there are 25 other charitable mission Blue Cross/Blue Shield insurers nationally who will be subject to the ACA (and are subject to Attorney General oversight) but are not claiming they have to convert?
- How much will it cost to convert BCBSM into a mutual? How much has been spent already? Is Blue Cross already paying for the consultants hired by the Department of Insurance?
- How do you reconcile Blue Cross's efforts to convert into a mutual insurer given the prohibition in its charter against exactly that action (see 550.1218)?¹ The charter also prohibits Blue Cross from taking any action that "results in a change in direct or indirect control" of Blue Cross, yet that will occur once policyholders become voting members. Did you receive a legal opinion as to the appropriateness of Blue Cross's actions in light of these express prohibitions? Would you be willing to make that public?

Other Governance Issues:

- Will policyholders be able to nominate and/or remove a member of the board?
- Will the mutual send a proxy statement to policyholders every year?
- Will the policyholders have the authority to propose and consider resolutions to the board?
- Have you asked for or received a legal opinion on the question of whether denying policyholders of ownership rights in the mutual's surplus is enforceable? Will you agree to make any such opinion public?
- Since mutual insurer's typically dividend excess surplus back to their policyholders, how will Blue Cross mutual make such distributions, if any?

¹ Specifically, the nonprofit health care corporation reform act, Act 350 of 1980, precludes Blue Cross from taking "any action" to change its "nonprofit status," or to "mutualize" or "that results in a change in direct or indirect control of the health care corporation..."

Michigan Health and Wellness Foundation Valuation:

- BCBSM's own advisors determined that its social spending mission was \$391 million per year. (See Avalere Health LLC report, January 2008). So how are the taxpayers of Michigan better off receiving up to \$83 million a year in "contributions," plus a purported \$100 million in state and local taxes (minus any tax write-offs)? Does this plan not reduce overall social mission spending in Michigan by over \$200 million per year?
- Is there any way the Foundation can be expected to replace the over \$200 million in lost social mission spending? Will older adults and persons with disabilities be harmed by that gap? If not, who will?
- Do you agree that the proposed \$1.5 billion in "contributions" is worth far less on a present value basis if paid out over 18 years? What is your calculation of its present value?
- Are these "contributions" tax deductible? If so, what will be the net amount of Blue Cross's contribution after taxes out of that \$1.5 billion? What tax rate are you assuming?
- Is there an enforceable obligation within statute for Blue Cross to pay the \$1.5 billion in contributions?
- Do you agree that the fair market value of Blue Cross exceeds its book value of \$3.4 billion? Do you know by how much it exceeds that value?
- Are you familiar with "guarantee stock" as a traditional means of financing mutual insurers when they are formed? Would BCBSM consider issuing guarantee stock to the Foundation as part of its conversion? Despite your claims that this is not a conversion of BCBSM, does BCBSM have any objections to issuing guarantee stock to the Foundation? Wouldn't that protect the full valuation amount for the Foundation while allowing BCBSM to retain its current capital?
- Do you agree that under the current bills, Blue Cross would not have to obtain a valuation and compensate Michigan for its charitable assets until over 50% of the parent mutual company was conveyed or sold? See SB 1293, § 5825(3). Do you agree that this "greater than" 50% trigger would not apply to the sale of a "greater than 50% beneficial ownership interest" in a downstream stock subsidiary, even one that accounts for most of Blue Cross's assets?
- How would you propose the state recapture assets transferred to a for-profit stock subsidiary that has sold shares on the market? Is that even possible?
- Won't establishing a fair market value prior to the conversion prevent potential future disputes as to valuation? What protections are you proposing be put in place to prevent future disputes as to valuation of the Blue Cross charitable assets?



Why Use Guarantee Stock?

Guarantee stock is a mechanism to provide a new mutual insurer with capital (other similar methods exist - such as surplus notes - but these really do not differ substantially from guarantee stock). Guarantee stock is a special sort of stock with limited rights that is issued to investors that provide start up capital to a mutual. In the case of Blue Cross, the investor would be the Foundation. Using this method, Blue Cross would issue special guarantee stock to the Foundation, which would be redeemed over time from the profits of the converted company until the value of the charitable assets is entirely paid out to the Foundation. This would allow Blue Cross to continue operating without reducing the capital it needs to operate and allow for the Foundation to be repaid over time. Obtaining an independent valuation would allow the Foundation to set a value on the guarantee stock it receives. Guarantee stock (or surplus notes if preferred) are already permitted in Michigan by Insurance Code Section 500.5430 (entitled "Capital funds; borrowing; repayment.") Section 500.5430 expressly provides that:

A mutual insurer ... may borrow or assume liability for the repayment of a sum of money sufficient to defray the reasonable expenses of its organization ... the sum shall be repaid with interest accrued in a manner and at a rate approved by the commissioner. The agreement under which the sum is obtained shall provide that any claim for its return shall be inferior and subordinate to all claims of and reserves for policyholders and creditors. Interest shall be paid and principal shall be retired only out of the surplus earnings of the insurer and with the approval of the commissioner whenever, in his or her judgment, the financial condition of the insurer warrants it, except that approval shall be withheld if repayment will reduce the surplus to an amount that is less than the amount determined adequate to comply with section 403. Any sum advanced shall not form a part of the legal liabilities of the insurer but until repaid all statements published by the insurer or filed with the commissioner shall show the amount remaining unpaid.

The key provisions of 500.5430 that makes it a useful tool:

- The Commissioner of Insurance must approve the repayment rate, ensuring that BCBSMI will have flexibility if the company suffers substantial losses or a considerable downturn.
- The Guarantee stock "claim" is subordinate to the claims of policyholders and creditors. This protects the policyholders.
- Interest and principal are repaid from the surplus earnings of the insurer.
- The funds provided by the guarantee stock are not legal liabilities.

Establishing guarantee stock and transferring it to the Foundation is the best way to create an obligation to repay BCBSM's charitable assets in a legally recognized and enforceable (but flexible manner) and will help protect the public.

